UNITED NATIONS

A

General Assembly

Distr.
GENERAL

A/46/5/Add.7
30 July 1991

ORIGINAL: ENGLISH

Forty-sixth session
Item 106 of the provisional agenda*

FINANCIAL REPORTS AND AUDITED FINANCIAL STATEMENTS, AND REPORTS OF THE BOARD OF AUDITORS

Interim report of the Board of Auditors on the United Nations Population Fund for the first year of the biennium 1990-1991**

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* A/46/150.

** The present document contains the interim report of the Board of Auditors on the United Nations Population Fund for the first year of the biennium 1990-1991. The financial report and audited financial statements for the biennium ended 31 December 1991 and the report of the Board of Auditors regarding the Fund will be issued as Official Records of the General Assembly, Forty-seventh Session, Supplement No. 5G (A/47/5/Add.7).

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LETTER OF TRANSMITTAL

2 July 1991

Sir,

I have the honour to transmit to you the interim report of the Board of Auditors on the United Nations Population Fund for the first year of the biennium 1990-1991, in accordance with paragraph 8 of General Assembly resolution 45/235 of 21 December 1990.

Accept, Sir, the assurances of my highest consideration.

(Signed) Heinz Günter ZAVELBERG
President of the Federal Court
of Audit of Germany
and Chairman,
United Nations Board of Auditors

The President of the General Assembly
of the United Nations
New York, NY

INTERIM REPORT OF THE BOARD OF AUDITORS

I. INTRODUCTION

1. In its resolution 45/235 of 21 December 1990, the General Assembly approved the changes in the financial procedures of the United Nations Population Fund (UNFPA), as recommended by the Governing Council in its decision 90/36. As a consequence, the Board of Auditors will issue its report on the financial statements and relevant schedules of UNFPA relating to the accounts for the financial period on a biennial basis, beginning with the biennium 1990-1991. The audit report on the current biennium will be submitted in 1992.

2. The General Assembly, in its resolution 45/235, as well as the Governing Council, in its decision 90/36, invited the Board of Auditors to issue a special report for the first year of a biennium through the Advisory Committee on Administrative and Budgetary Questions if, in the opinion of the Board, there were matters that needed to be brought to the attention of the Governing Council and/or the General Assembly.

3. The Board of Auditors herewith issues an interim audit report on UNFPA to convey information on observations during the first year of the current biennium 1990-1991. The primary objective of the present report is to provide more up-to-date information in order to facilitate decision-making and to expedite the taking of prompt remedial action. Furthermore, the preparation of the interim report presents an opportunity to focus more strongly on management issues that, although included in the normal practice of auditing, in the process of regular reporting are often likely to fall short of receiving adequate consideration. Accordingly, the following sections pay particular attention to such aspects as economy and efficiency.

4. The Board of Auditors continued its normal practice of reporting the results of specific audits at headquarters and in the field and of issuing management letters to the administration. The audits were carried out in accordance with article XII of the Financial Regulations of the United Nations and the annex thereto and with the common auditing standards adopted by the Panel of External Auditors of the United Nations, the specialized agencies and the International Atomic Energy Agency (IAEA). All observations included in the present report were discussed with the administration and comments provided by the latter are reflected in the report where appropriate.

II. FOLLOW-UP ON ACTIONS TAKEN ON PREVIOUS AUDIT RECOMMENDATIONS

5. The Board noted that some action was taken on the recommendations made by the Board in its audit report for the year ended 31 December 1990. The details and comments of the Board thereon are outlined in the annex. Summarizing, the Board wishes to emphasize, however, that further efforts are needed. In particular, there are still no adequate procedures in place to obtain audited statements of executing agencies in time for the audit and final issuance of the audit opinion on the financial statements of UNFPA. Consequently, the audit opinion will once again be qualified unless the situation changes.

III. SUMMARY OF RECOMMENDATIONS

6. We recommend that the following corrective actions, presented in order of priority, be taken:

(a) Means should be established to ensure that non-governmental organizations receive support costs on an equal scheme of assessment and on the basis of actual project expenditures (para. 21);

(b) A clear distinction and separation between direct and indirect administrative support costs should be made to ensure that no unjustified payments for administrative support by non-governmental organizations occur (para. 26);

(c) Further steps should be taken to enhance the control of interest income earned by executing agencies on funds provided by UNFPA (para. 45);

(d) Provisions should be established warranting that the purpose, scope, duration and necessary inputs of any pre-project activities be specified precisely (para. 30);

(e) The approval authority for pre-project activities should be restricted with regard to the financial volume and the scheduled duration of the actual projects (para. 34);

(f) The existing provisions governing the designation and execution of certifying and approving functions in the field should be revised (para. 40);

(g) The execution of supervisory functions by headquarters regarding the certifying and approving functions in the field has to be strengthened (para. 40).

IV. SUMMARY OF FINDINGS

7. The practice of reimbursing overhead costs to non-governmental organizations is not in line with UNFPA Financial Regulations and Rules, which state that the calculation of such costs shall be within the limits established by the Governing Council (paras. 17 and 18).

8. Support activities are not paid to non-governmental organizations on an equal scheme of assessment and on the basis of actual project expenditures (paras. 19-21).

9. Expenditure control is rendered unnecessarily difficult or even impossible owing to the insufficient availability of information about the calculation of overhead costs of non-governmental organization projects (para. 22).

10. In addition to the overhead costs paid to non-governmental organizations, UNFPA also reimburses them for administrative costs directly allocated to individual projects. No clear distinction and separation between these costs exist (paras. 23-26).

11. The circumstances under which funds for pre-project activities may be approved are not clearly defined and specified with regard to purpose, scope and necessary inputs (para. 27-30).

12. No precautions are in place warranting that the proportion of pre-project activities remain within reasonable limits with respect to the financial volume and the duration of the intended project itself (paras. 31-34).

13. The designation and execution of certifying and approving functions in field offices was found to have flaws in numerous cases. The execution of supervisory functions by headquarters in this respect showed considerable weaknesses (paras. 35-37).

14. The guidelines governing the relationship between the United Nations Development Programme (UNDP) and UNFPA in the field and related directives are ambiguous and inconsistent with regard to certifying and approving functions (paras. 38-40).

15. The closing balance of the operating fund accounts with Governments is still high. The total of advances paid to Governments permanently exceeds the actual needs of the implementing agencies by approximately 20 per cent (paras. 41-43).

16. In spite of high advances, very little interest income is reported by recipient Governments. The same applies for intergovernmental institutions and agencies, including non-governmental organizations (paras. 44-48).

V. FINDINGS

A. Agency support costs paid to non-governmental organizations

17. According to UNFPA's statement of expenditure, the share for agency support costs, which are regarded as overhead costs and paid by UNFPA to intergovernmental institutions and other agencies, including non-governmental organizations, increased from $183,529 in 1986 to $1,285,711 in 1990. This represents an increase of more than 600 per cent. During the same period, the corresponding programme expenditure increased by only 64 per cent. This disproportionate increase led the Board to review the existing policies and procedures in this respect. The following paragraphs refer to agency support costs paid to non-governmental organizations.

18. As required by UNFPA financial regulation 8.7, non-governmental organizations may be reimbursed for their support costs up to levels determined by the Governing Council. In addition, the UNFPA Policy Guideline for Assistance to Non-Governmental Organizations (UNFPA/CM/86/65) lays down that the question of overhead and administrative costs will be considered on a case-by-case basis, as necessary, but such costs shall be within the limits established by the Governing Council. However, the Board could not find evidence that any such limits were established by the Governing Council. Instead, specifications in project documents and memoranda of understanding between UNFPA and the recipient non-governmental organization served as the only basis for the payment of agency support costs.

19. For the time being, non-governmental organizations are not reimbursed for administrative support on an equal scheme of assessment. The audit revealed that overhead rates differed from one non-governmental organization to another, and even between individual projects executed by the same organization, with rates ranging from 0 to 35 per cent, and in some cases up to 140 per cent of the project costs. Most of the overhead costs were calculated and refunded on the basis of budgeted project expenditures or advance payments relating to previous or succeeding periods rather than on the basis of actual project expenditures.

20. Management admitted that the guideline mentioned above was incomplete and may be misleading. It should have said that such costs shall be within the limits as may be established by the Governing Council. Management pointed out that the subject of UNFPA successor arrangements for agency support costs was to be discussed at the thirty-eighth session of the Governing Council and that management would discuss that issue once a decision had been reached by the Governing Council.

21. The Board wishes to underline that the proposed successor arrangements for agency support costs submitted to the Governing Council do not deal with the issue of support costs to non-governmental organizations under consideration. In the opinion of the Board, this issue needs clarification in order to ensure that the various non-governmental organizations receive their overhead costs on an equal scheme of assessment and on the basis of actual project expenditures.

22. The Board further noted that detailed information about the calculation of support costs regularly are only known to the project management that deals with the particular project. This situation impedes comparative analyses and renders financial controlling, especially regarding the performance of certifying payments, unnecessarily difficult or even impossible. The Board recommends facilitating the financial control by providing more detailed information about the period the overhead costs refer to, the calculation base (actual expenditure or allocation) and the overhead rate.

B. Reimbursement of direct administrative costs to non-governmental organizations

23. Besides the agency support costs set out in the financial statements (i.e. the overhead indirect administrative costs of projects), UNFPA also reimburses non-governmental organizations for administrative costs incurred for and directly allocated to individual projects. The costs directly allocated to projects are prorated on the basis of the non-governmental organizations' actual costs and, after negotiation with the respective organization, included into the project budget, thus adding on to the administrative costs of UNFPA programme activities (for example, more than $500,000 in 1990).

24. To ensure that non-governmental organizations will not be reimbursed more than once for expenditures incurred for administrative activities, a clear distinction and separation between direct and indirect costs and a correct relating of such costs to the relevant accounting period is required. However, no adequate means are in place for this purpose.

25. Management replied that most, if not all, of the arrangements with non-governmental organizations included a combination of indirect and direct administrative costs. Negotiating this tended to be time-consuming but offered the advantage of transparency. Both direct and indirect costs were reflected in the budget allocations to non-governmental organizations. However, in both instances costs to UNFPA were assessed on the basis of actual expenditure, because allocations of overhead costs were based on the budget estimated with reconciliation made in the course of financial reporting.

26. In the view of the Board, this explanation is questionable. A verifiable calculation, including the direct costs as well as the indirect costs that are charged as support costs, was only noted in one case. No balancing entries could be identified in the relevant ledger accounts indicating a reconciliation of budget estimates with actual expenditure in this respect. The Board is of the opinion that administration should take appropriate measures to ensure that no unjustified payments for administrative support by non-governmental organizations occur.

C. Pre-project activities

27. In order to give recipient Governments sufficient time to become fully involved in the preparation of project requests, pre-project activities or preparatory assistance may be approved for periods of up to one year during which funds can be expended, e.g. for training, technical advisory services,

consultancies, study tours or the purchase of project equipment and supplies. The country director is given approval authority for requests for pre-project activities provided that the total costs for the project, including preparatory activities, do not exceed $500,000. This concept is reflected in various circulars (e.g. UNFPA/CM/88/61, UNFPA/CM/88/63 and UNFPA/88/40/Rev.2).

28. The Board is of the opinion that the current directives regarding pre-project activities may constitute a commitment of UNFPA to a proposed project before a final agreement on the project is accomplished. If, for any reason, a proposed project for which pre-project activities were undertaken subsequently is not approved or implemented, it may be difficult to terminate pre-project activities and to get back advance payments already transferred. The exceptional circumstances under which preparatory assistance funds may be approved are not clearly defined and specified with respect to purpose, scope and necessary inputs of pre-project activities. Moreover, the instructions lack clear distinction between pre-project activities and so-called umbrella projects in so far as the latter may also be used for such preparatory purposes, for example, developing a programme/project design.

29. The administration commented that it had already established guidelines and criteria on the approval of such activities, but failed to indicate where these criteria were laid down. Although the administration did not share completely the Board's concern with regard to the financial risk involved in preparatory assistance, it agreed that there was a need to consolidate UNFPA procedures.

30. The Board recommends a precise specification of the scope, the duration and the necessary inputs of pre-project activities, including a clear delineation between preparatory assistance and umbrella projects. Accordingly, a comprehensive circular on this topic should be issued and distributed without delay to field offices, participating and executing agencies, as well as to professional staff at headquarters.

D. Arrangements for long-term advisers as pre-project activities

31. Circular UNFPA/CM/89/11 authorizes the geographical division chiefs at headquarters to approve and allocate resources for advisers on a long-term basis (12 to 24 months). They are instructed to designate the approval as a pre-project activity. This instruction, however, does not conform with the principle of approval authority for up to one year as mentioned above and may cause inconsistencies, as illustrated below.

32. The Government of one country, inter alia, requested an international expert for an intended three-year project on family life education with estimated costs of $255,600 (CHD/89/P03). According to the records, the expert was supposed to serve as chief technical adviser for the future project. The Project Review Commission at headquarters approved the post for a period of 24 months (1990-1992) as a pre-project activity and allocated a total amount of $200,000 for reasons that could not be seen from the records.

33. As expenditures for pre-project activities have to be deducted from the future project budget, the Project Review Commission's approval and allocation actually constituted a commitment of nearly 80 per cent of the total project costs estimated. Moreover, the approval to recruit the expert for a period of two years comes close to an irrevocable decision in favour of the project, because two thirds of the project's duration will end before the expert's assignment is completed.

34. In the opinion of the Board this procedure is not in compliance with the idea of pre-project activities. Approval of pre-project activities should not be given other than under the explicit provision that these are only to establish appropriate conditions for the realization of the main project. Funds and time involved should only require a small share of the total resources committed to a project and, accordingly, the approval authority for preparatory assistance should be restricted to a rather limited percentage of the respective budget line for the project. The Board recommends reviewing the pertinent provisions.

E. Internal financial control

35. The Executive Director shall, for the purpose of internal financial control, designate certifying and approving officers. The main responsibilities of certifying officers are to certify that the supporting documents are correct, that proposed expenditure is in concurrence with existing policies, regulations and rules, that authority for the expenditure exists and that funds are available. The responsibility of approving officers is to approve payments or obligations to be incurred. As a basic principle of internal financial control, certifying and approving functions must not be carried out by the same staff.

36. During its audits, the Board focused, inter alia, on the designation and execution of certifying and approving functions in field offices. The audits, which also included an evaluation of findings of the internal audit, revealed numerous deficiencies. In particular, the Board noted that pertinent provisions for certifying and approving functions request a "specific authorization" by UNFPA headquarters without, however, further elucidating this. The Board was unable to get clarification either in the field or at headquarters as to what precisely that "specific authorization" meant and implied. In the various field offices audited no documentation of such authorization could be found as a valid basis for the discharge of such functions.

37. The Board further noted considerable weaknesses regarding the execution of supervisory functions by headquarters. Headquarters was unable to provide a complete and up-to-date list of UNFPA approving and certifying officers in the field when requested to do so and had either to call for a list available at UNDP headquarters or to ask UNFPA field offices to provide the relevant information.

38. The Board examined in more detail the consistency of the guidelines entitled "UNDP/UNFPA Relationship in the Field and Arrangements of UNFPA Field Offices" as at 1 March 1990, as well as related provisions. The guidelines

establish, inter alia, basic principles with respect to the assignment and execution of certifying and approving functions in the field.

39. The guidelines, although in keeping with previous comments of the Board repeatedly amended by circulars, still contain considerable flaws, such as the description of the certifying functions referring to a UNDP memorandum that is not applicable any more, the unrestricted authority given to UNDP resident representatives to delegate their approving function to other field officers and the ambiguity as to whether the UNFPA country director is supposed to be certifying officer ex officio or only by specific appointment.

40. The Board is of the opinion that clear and unambiguous provisions in guidelines and directives are a precondition for the proper and efficient performance of administrative procedures. Certifying and approving functions being a basic internal financial control mechanism, the Board considers revising the existing system of provisions and eliminating the numerous unclear points and deficiencies a matter of utmost urgency. Furthermore, the Board is of the opinion that the execution of supervisory functions by headquarters regarding the certifying and approving functions in the field has to be strengthened.

F. Controlling of potential interest income

41. Financial provisions stipulate that funds released to Governments for UNFPA projects should approximately equal the cash requirement for the ensuing period less the estimated unexpended balance carried over from the previous period.

42. As at 31 December 1990, the closing balance of the operating fund accounts with Governments was $6.6 million, compared to $9.0 million at the end of 1989. There seems to be an improvement in reducing the unexpended balance of advanced payments, but a three-year in-depth review revealed the still poor and delayed disbursement reporting. The closing balances of some countries and projects were higher than desirable. A number of project accounts, in an amount of approximately $442,000, were carried over from the previous financial period and have remained outstanding until the end of the year.

43. It was obvious that some Governments were obtaining more advances from UNFPA than they actually needed to cover the local project costs for the periods intended. Approximately 20 per cent of the total available advances paid seem to exceed permanently the actual needs of the implementing agencies. In such cases, funds could be invested to generate additional income from interest for non-budgeted activities. A significant case of that kind was mentioned by the Board in its report for 1989 (para. 144). The administration agreed that greater efforts could be expended to reduce further the balance of outstanding cash advances, but doubted the practicability of mandating further drastic measures.

44. In spite of the high advances only very little interest income was reported by the recipient Governments. The level of cash advances to the implementing agencies as well as the expenditure reported by them are recorded

in the operating fund account. However, no procedure exists to control a possible build-up of income from interest earned on UNFPA funds.

45. The Board finds it difficult to believe that all the advances are held on non-interest-bearing accounts. The Board is of the opinion that further steps by the administration are urgently needed to enhance the control of potential interest income, for instance, by:

(a) Making special inquiries in cases in which no interest income was reported although significant advances are still outstanding;

(b) Insisting on statements duly audited;

(c) Requesting reconciliation of bank statements showing the amount of interest earned on UNFPA funds;

(d) Introducing appropriate measures to enforce compliance with established provisions.

46. The Board further noted that the advances outstanding at year-end closing are maintained under the advance code on microfiches, but clearing and liquidation of the advances are executed manually. Since manual verification is excessively time-consuming and not practical, the Board recommends that the relevant data available at headquarters be used to estimate the potential interest income that might have been earned if such advances had been deposited in interest-bearing accounts.

47. The Board learned from the statements of non-governmental organizations, for which no operating fund accounts are maintained, that here too high advances were given but very little interest income was reported. To facilitate locating and verifying if interest income was earned on UNFPA funds, the Board considers it indispensable that non-governmental organizations be committed to operating a separate bank account and to maintaining an interest-bearing account for the receipt and disbursement of UNFPA funds. The administration pointed out that, according to financial regulation 15.1, non-governmental organizations might carry out UNFPA projects under their respective financial provisions and thus the imposition of requirements by UNFPA was restricted.

48. The Board takes note of the administration's assurance that it will actively consider certain recommendations of the Board. The Board recommends that UNFPA further tighten administrative controls on outstanding cash advances, both for Governments as well as non-governmental organizations.

VI. ACKNOWLEDGEMENT

49. The Board of Auditors wishes to express its appreciation for the cooperation and assistance extended by the staff of the United Nations Population Fund.

(Signed) Heinz Günter ZAVELBERG
President of the Federal Court
of Audit of Germany

(Signed) Eufemio C. DOMINGO
Chairman, Commission on Audit
of the Philippines

(Signed) Osei Tutu PREMPEH
Auditor-General of Ghana

Annex

FOLLOW-UP ON ACTIONS TAKEN ON PREVIOUS AUDIT RECOMMENDATIONS

Recommendation 6 (a) of the 1989 Board report

1. The Board had pointed out that further efforts are needed and, in particular, that adequate procedures should be designed and implemented to obtain audited statements of executing agencies in time for the audit and final issuance of the audit opinion on the financial statements of UNFPA.

Measures taken by the administration

2. In the view of the administration, the change to the biennial presentation of the financial statements approved by the Governing Council in its decision 90/36 will result in an unqualified opinion on this matter, provided that audit certificates from the auditors of the executing agencies are received prior to the completion of the UNFPA biennial audit.

3. The administration pointed out that, in 1990, it had issued a set of year-end financial closing instructions to all the United Nations executing agencies to whom UNFPA had entrusted projects, with the intention to assist those agencies to produce financial reports for UNFPA projects in an expedient manner.

4. Regarding Government-executed projects, the administration stated that it had taken steps to try to improve Governments' rate of compliance with UNFPA financial policies and procedures, such as organizing field consultations, dispatching instructions to field offices and holding briefing sessions at headquarters. Effective 1991, a computer software package would be used to monitor compliance of Governments with their auditing responsibilities. In addition, the administration will seek authorization to establish a UNFPA Internal Audit Unit to, inter alia, monitor the level of audit compliance of Government-executed projects.

5. With regard to non-governmental organizations, intergovernmental institutions and other agencies, the administration pointed out that it had, in December 1990, issued year-end financial closing instructions to all non-governmental organizations with a view to assisting them to fulfil their year-end financial reporting requirements. In addition, effective January 1991, it would follow a policy of reimbursing organizations for the costs of independent audits when they were unable to comply with UNFPA audit requirements owing to financial constraints.

Findings and comments of the Board of Auditors

6. The Board welcomes the steps taken to consider and implement the Board's recommendations, but wishes to point out that, for close to one quarter of the UNFPA funds spent by Governments and non-governmental organizations, audited financial reports for 1989 were still not available in the spring of 1991. Based on the experience with the interim financial statements as at 31 December 1990, the Board questions whether the measures taken will result

in a timely submission of audited statements by the executing agencies in the future. The Board wishes to emphasize that the audit opinion on the UNFPA financial statements will remain qualified until sufficient audit substance is obtained in due time for expenditures incurred by executing agencies.

Recommendation 6 (b) of the 1989 Board report

7. The Board recommended that the financial control regarding balances of advances to Governments should be improved.

8. The administration stated that further measures were taken to help ensure full compliance with the requirement for clearing advances to Government-executed projects. It indicated, however, that although UNFPA had taken significant steps to help ensure increased accountability and control in project execution, without the full cooperation of the Governments the Board's concern regarding the level of cash advances in the hands of Governments might remain.

Measures taken by the administration

9. The administration specified that a manual concerning the accounting, financial reporting and auditing policies and procedures for Government-executed projects was developed and distributed as a draft to UNFPA field offices. Training programmes would be continued to enhance the competence of UNFPA and government staff in dealing with Governments' financial reporting and auditing responsibilities. The Executive Director would present to the Governing Council proposals including the establishment of new local posts aimed at strengthening the capacity of UNFPA-financed projects. In this connection, the administration stressed that the increase in the number of Government-executed projects and the attendant need for systematic processing of information from projects had had a significant impact on the accounting and financial monitoring workload of UNFPA.

Findings and comments of the Board of Auditors

10. The unspent balances of advances have decreased from $9 million as at 31 December 1989 to $6.6 million as at 31 December 1990. However, it is too early to conclude whether the depicted measures will eventually lead to an acceptable low level of unspent cash advances. The Board is of the opinion that UNFPA should continue its efforts to conduct dialogues with Governments and to clear the outstanding advances on a regular and timely basis.

11. The Board, for the time being, is not in a position to comment on whether the establishment of new posts intended by the administration is justified and necessary with respect to this question, but will focus on it in its future audits.

Recommendations 6 (c and d) of the 1989 Board report

12. The Board reiterated its former recommendation that comprehensive guidelines in order to clarify the delineation between programme, programme support and administrative expenditure should be issued. The Board further recommended that guidelines be issued to ensure consistent handling of the approval and execution of all kinds of official travel.

Measures taken by the administration

13. The administration in its comments elaborated in detail on its views on the factors determining whether a certain UNFPA publication should be included in the administration and programme support services budget or financed from project funds. As regards official travel, guidelines for official UNFPA travel were issued in 1990 (UNFPA/CM/90/79, dated 18 October 1990) and a revision was made in 1991. The guidelines, in the administration's opinion, highlight the criteria to be used when deciding which funds should be used.

Findings and comments of the Board of Auditors

14. The measures taken only cover a small area. They cannot be considered sufficient to provide the necessary general clarification as to the delimitation between programme, programme support and administrative expenditure. Clear and precise definitions with respect to these different kinds of expenditures in all areas seem indispensable to ensure correct accounting.

15. The Board appreciates that the travel guidelines, originally issued mainly to facilitate the planning and the decision-making process on the official travel of UNFPA staff members, now also refer to other kinds of travel and, furthermore, stipulate the approval and setting up of an annual travel plan procedure. Whether or not the travel guidelines will ensure consistency in handling all travels cannot yet be assessed. With respect to the source of funding of travel costs, the Board maintains that the guidelines should further specify whether travel costs of headquarters staff participating in an evaluation mission are to be reported as administrative or project costs, and whether the costs related to the participation of agencies' staff in back-stopping missions are project costs or programme support costs.